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In the Supreme Court of the United States

OCTOBER TERM, 1987

NATIONWIDE CORPORATION AND NATIONWIDE MUTUAL INSURANCE COMPANY, PETITIONERS

v.

HOWING COMPANY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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QUESTION PRESENTED

Whether shareholders have a private right of action for damages caused by violations of the proxy disclosure requirements of the Securities and Exchange Commission's Rule 13e-3, 17 C.F.R. 240.13e-3, which applies to "going private" corporate transactions.

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BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

This brief is filed in response to the Court's invitation to the Solicitor General to express the views of the United States.

STATEMENT

1. In 1982, petitioner Nationwide Mutual Insurance Company (Nationwide Mutual) owned 85.6% of the outstanding Class A common shares of petitioner Nationwide Corporation (Nationwide); the remaining Class A shares were owned by the public. In September 1982, officers of Nationwide Mutual approached the president of Nationwide and proposed that Nationwide Mutual purchase the publicly held shares of Nationwide. In November of that year, the Board of Directors of Nationwide approved a merger transaction in which the owners of Nationwide's publicly held Class A shares would receive $42.50 per share for their shares, and which would result

in Nationwide Mutual and an affiliate owning 100% of a successor to Nationwide. Pet. App. 4a.

On December 9, 1982, Nationwide issued a proxy statement soliciting votes of Nationwide shareholders to approve the merger transaction (Pet. App. 42a). The proxy statement declared that, if the public shareholders voted against the proposed merger, Nationwide's board of directors might reconsider the transaction (*id.* at 65a). The merger transaction, however, was approved by 94.7% of the voted public shares, and the transaction was consummated (*id.* at 43a).

2. Respondents, who were public shareholders of Nationwide prior to the merger, brought this action against petitioners. Respondents alleged, inter alia, that Nationwide's proxy statement violated Securities and Exchange Commission (SEC) Rule 13e-3, 17 C.F.R. 240.13e-3. Rule 13e-3 and Item 8 of Schedule 13E-3, 17 C.F.R. 240.13e-100, require an issuer to state, in a proxy statement soliciting approval of a "going private" merger, whether the issuer believes that the transaction is fair to shareholders, and to "[d]iscuss in reasonable detail the material factors upon which [such] belief" is based. Item 8 also requires the proxy statement to discuss the weight assigned to each factor. This informaton must be "set forth prominently" in a "Special Factors" section of the proxy statement. See Rule 13e-3(e)(3)(i), 17 C.F.R. 240.13e-3(e)(3)(i). The instructions to Item 8 caution that "[c]onclusory statements, such as '[T]he Rule 13e-3 transaction is fair to unaffiliated security holders in relation to net book value, going concern value and future prospects of the issuer' will not be considered sufficient disclosure in response to Item 8(b)" (17 C.F.R. 240.13e-100). Respondents alleged that Nationwide's proxy statement failed to provide more than conclusory statements.

3. The district court entered summary judgment in favor of petitioners. Without discussing whether petitioners have an implied private right of action for damages in these circumstances, the district court held that Nationwide's proxy statement satisfied the disclosure requirements of Rule 13e-3 (Pet. App. 58a). In particular, the court stated (*id.* at 54a) that the proxy statement adequately disclosed the bases for the conclusion of Nationwide's independent directors that the merger was fair.

The court of appeals reversed the district court's judgment (Pet. App. 1a-25a). The court first held that an implied right of action exists under Section 13(e) of the Securities Exchange Act (15 U.S.C. (& Supp. IV) 78m(e)) for violations of Rule 13e-3 (Pet. App. 8a-13a). The court then agreed with respondents that Nationwide's proxy statement violated Rule 13e-3 because it failed to disclose required information relating to the fairness of the transaction (Pet. App. 16a-19a).[1] The court declared that "defendants have done nothing more than provide a laundry list of factors considered by their investment banker" and have made "precisely the kind of conclusory statements prohibited by the Rule" (*id.* at 17a-18a (footnote omitted)). The court of appeals remanded the case for a determination whether the omitted information was material (*id.* at 24a-25a).[2]

DISCUSSION

The court of appeals in this case answered a question (Pet. App. 8a-13a) it did not need to reach: whether

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[1] The court of appeals stated that Nationwide's disclosure was "woefully inadequate" (Pet. App. 19a).

[2] The court of appeals rejected respondents' claims that Nationwide omitted other information required by Schedule 13E-3 and violated the antifraud provisions of SEC rules. See Pet. App. 15a-16a, 19a-24a.

shareholders have an implied cause of action for damages for violations of Section 13(e) of the Exchange Act, which governs an issuer's purchases of its own securities. Whatever the answer to that question may be, there is no doubt about the availability of a shareholder damage action here: the conduct alleged in this case violated Section 14(a) of the Exchange Act (15 U.S.C. 78n(a)), under which a cause of action in favor of shareholders such as respondents is firmly established. Because Section 14(a) and this Court's cases fully support the decision below, further review is not warranted.

1. Section 14(a) of the Exchange Act makes it unlawful "to solicit any proxy" in "contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." In *J.I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), this Court held that shareholders have an implied right of action for damages under Section 14(a) for violations of the Commission's proxy rules. As the Court noted in *Borak*, "[t]he purpose of § 14(a) is to prevent management or others from obtaining authorization for corporate action by means of deceptive or inadequate disclosure in proxy solicitation" (377 U.S. at 431). The Court emphasized that Section 14(a) was intended to benefit shareholders and that "[p]rivate enforcement of the proxy rules provides a necessary supplement to Commission action" (377 U.S. at 432). The Court has twice reaffirmed its holding in *Borak*. See *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438 (1976); *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970).[3]

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[3] Numerous lower courts have recognized the continuing validity of *Borak*. See, *e.g.*, *Palumbo* v. *Deposit Bank*, 758 F.2d 113 (3d Cir. 1985); *Cowin* v. *Bresler*, 741 F.2d 410 (D.C. Cir. 1984); *Rauchman* v. *Mobil Corp.*, 739 F.2d 205 (6th Cir. 1984); *Haas* v. *Wieboldt Stores*,

The transaction in this case fell within the Commission's Rule 13e-3, which governs many aspects of "going private" transactions in which an issuer or an affiliate purchases the issuer's securities. As relevant to this case, Rule 13e-3 specifies certain information that must be included (along with the information required by various other Commission rules) in a proxy statement seeking approval of a "going private" transaction. The Commission adopted those specific disclosure requirements (involving matters such as the history, purpose, and fairness of the transaction) because, in the context of "going private" transactions, minority shareholders need especially particularized information in order knowingly to exercise their options. See Exchange Act Release No. 14185, 13 S.E.C. Dkt. 839, 841-843 (Nov. 17, 1977).

The court of appeals held that Nationwide's proxy statement violated Rule 13e-3 because it omitted information concerning the fairness of the merger transaction. The petition does not seek review of that holding.[4] By violating the proxy statement requirements of Rule 13e-3, Nationwide violated Section 14(a) of the Exchange Act; Nationwide solicited proxies "in contravention of [the] rules and regulations [of] the Commission" (15 U.S.C. 78n(a)). Accordingly, it follows from *Borak* that respondents may have a claim for damages under Section 14(a).

2. This conclusion is not affected by the fact that the Commission included certain of the proxy requirements relating to "going private" transactions in "Rule 13e-3" in-

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Inc., 725 F.2d 71 (7th Cir. 1984); *Lebhar Friedman, Inc.* v. *Movielab, Inc.*, [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,162 (S.D.N.Y. 1987); *Lynch* v. *Fulks*, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,831 (D. Kan. 1980).

[4] We therefore assume that the court of appeals correctly decided that Nationwide's proxy statement violated Rule 13e-3.

stead of a rule with the prefix "14a" to correspond to Section 14(a) of the Exchange Act. In promulgating Rule 13e-3, the Commission expressly relied on Section 14(a) of the Exchange Act (see Exchange Act Release No. 16075, 17 S.E.C. Dkt. 1449, 1470 (Aug. 2, 1979)), which gives the Commission plenary authority to adopt proxy rules "in the public interest and for the protection of investors."[5] The Commission chose not to label its "going private" rule with a "14a" prefix because the rule relies on many provisions of the securities laws and governs matters in addition to proxy solicitations (*e.g.*, tender offers, exchange offers, and open-market purchases). But Rule 13e-3 contains explicit proxy statement requirements—it provides that specified information "shall be included in the proxy statement" (17 C.F.R. 240.13e-3(e)(1)). Nationwide's failure to comply with those requirements was a solicitation of proxies in violation of Section 14(a) of the Exchange Act.

Petitioners suggest (Pet. i) that there is a private cause of action under Section 14(a) only for false or misleading statements in violation of Rule 14a-9, 17 C.F.R. 240.14a-9. We are not certain whether they mean to say that there should be a distinction between affirmative misrepresentations and deceptive omissions (both of which are considered fraudulent) or whether they intend to suggest a distinction between misleading statements, on the one hand, and failure to include specific disclosures required by Commission rules, whether or not such an omission renders the proxy statement deceptive. Petitioners are wrong on both distinctions. Although *Borak* itself involved an affirmative misstatement, nothing in Section 14(a) or the *Borak* line of cases suggests any distinction between different kinds of violations of Section 14(a), and certainly not a distinction between misrepresentations and

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[5] Nothing in Section 13(e) of the Exchange Act limits this authority.

deceptive omissions. Indeed, the Court in *Mills* v. *Electric Auto-lite Co., supra,* predicated liability upon an *omission* from a proxy statement of the fact that the board of directors that recommended approval of a merger with Mergenthaler Linotype Co. was controlled by Mergenthaler.

Section 14(a) makes it "unlawful" to solicit proxies in a manner that violates any of the Commission's proxy rules, not merely the rules prohibiting false or misleading representations. The Court said in *Borak* that the sweeping language of Section 14(a) was intended to prevent "deceptive or *inadequate* disclosure in proxy solicitation" (377 U.S. at 431 (emphasis added)). Thus, the omission from a proxy statement of information required by the Commission's rules for the protection or assistance of investors is a violation of Section 14(a) for which injured shareholders have a cause of action, whether or not that omission results in a document that is deceptive.

The Seventh Circuit recently rejected the argument that there is a private right of action under Section 14(a) only for misrepresentations. In *Haas* v. *Wieboldt Stores, Inc.*, 725 F.2d 71 (7th Cir. 1984), the court held that there is a private damages remedy for violation of Rule 14a-7, 17 C.F.R. 240.14a-7, which requires a corporation to mail a shareholder's proxy materials to shareholders. The court stated: "[A]lthough the precise rule in question [in *Borak*] was 14a-9, which forbids misleading proxy materials, rather than 14a-7, we cannot find anything in the Court's opinion, nor can think of any reason ourselves, that would justify a different treatment of the two rules" (725 F.2d at 73). See also *Rauchman* v. *Mobil Corp.*, 739 F.2d 205 (6th Cir. 1984) (assuming that there is an implied private action under Rule 14a-8, 17 C.F.R. 240.14a-8, which governs the inclusion of shareholder proposals in a corporation's proxy statement); *New York City Employees' Retirement System* v. *American Brands, Inc.*, 634 F. Supp. 1382

(S.D.N.Y. 1986) (shareholders have private cause of action for violations of Rule 14a-8). The court of appeals in this case, therefore, clearly reached the correct result: there is a private right of action for noncompliance with the disclosure requirements for proxy statements that are set forth in Rule 13e-3.[6]

In coming to that conclusion, the court decided an issue of first impression in the courts of appeals that it did not need to resolve—*i.e.*, whether there is a private right of action under Section 13(e) of the Exchange Act.[7] The court stated that there is such a right of action, and petitioners seek review of that declaration; but whether or not the court gave the correct answer to that question, the result reached below in this case was correct. Under Section 14(a) and this Court's decisions, respondents have a cause

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[6] The court of appeals also correctly remanded the case to the district court for a determination whether the omitted information was material. The Court stated in *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 385 (1970), "[w]here there has been a finding of materiality, a shareholder has made a sufficient showing of causal relationship between the violation and the injury for which he seeks redress * * *." As the Court explained in *Mills*, the requirement of materiality "serves the purpose of ensuring that a cause of action cannot be established by proof of a defect so trivial, or so unrelated to the transaction for which approval is sought, that correction of the defect or imposition of liability would not further the interests protected by § 14(a)" (396 U.S. at 384).

[7] The district courts are split on this issue. One district court has held that there is a private right of action for damages for violations of Section 13(e). See *Fisher* v. *Plessey Co.*, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,246 (S.D.N.Y. 1983). Two other district courts disagree. See *Berg* v. *First American Bankshares, Inc.*, [1984-1985 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,011 (D.D.C. 1985); *Kalmanovitz* v. *G. Heileman Brewing Co.*, 595 F. Supp. 1385 (D. Del. 1984).

of action for Nationwide's violation of the Commission's regulations governing the content of proxy statements. Since a different answer to the question about remedies under Section 13(e) would not affect the outcome of this case, no further review is warranted.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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